



16 JUN 1978

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Contract

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MEMORANDUM FOR: Director of Central Intelligence

VIA: General Counsel

FROM: John F. Blake
Deputy Director for Administration

SUBJECT: Security Provisions in Agency Contracts

REFERENCES: (a) Memo to DCI, dtd 1 Jun 78, fm DDA,
no subject (DD/A 78-2042/1)

(b) Memo to DDA, dtd 6 Jun 78, fm DCI,
Subject: Contracting Procedures on
Security (ER 78-1465/3)

1. Reference (a) was an update on the status of actions we are taking in the area of industrial security. Reference (b) indicated your concern with the development of a "performance clause" which would subject a contractor to penalties in the event of a leak of security information.

2. It appears that we are involved in uncharted waters when we attempt to use a penalty approach in Government contracting to enforce security requirements. While we can say with absolute certainty that a contractor is contractually required to meet all the security requirements of his contract, the legal mechanisms to enforce performance have not been tested by Boards of Contract Appeals or in the Courts. The Office of General Counsel has found no cases in which a contract has been terminated for default based upon a violation of security.

3. The legal bases for attributing the acts of an agent (employee) to his principal (contractor) are well established in Government contracting. If a contractor cumulatively fails to live up to the standard of duty required in: (1) the selection of the employee who is given access to classified information; (2) the method of training of that employee; (3) the method and character and intensity of supervision of that employee; and, (4) enforcement of the contractor's own policy and procedures

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with respect to handling classified material, his liability for the employee's actions can be affixed under the heading of either lack of good faith or willful misconduct. The burden of proof in this regard would be with the Government. Inasmuch as we approve the contractor's security procedures and grant approvals for persons to be given access to classified data, the possibility for our shifting the total responsibility to the contractor for a breach of contract for a security violation by one of his employees is rather remote.

4. Specific contract penalties, outside the very drastic step of termination for default, are also difficult to assess. The Task Force on Industrial Security and Industrial Contracting in Recommendation No. 17 of its Interim Report suggested "That incentive award fee type contracts include security performance along with other performance requirements as a basis for fee determination." This concept, which you approved, can be implemented to provide reward/penalty for various levels of contractor performance. While there are reasons other than profit on an instant contract which motivate a contractor to do a good job, a portion of an award fee, associated with security, could provide a meaningful incentive to a contractor. The rewards and penalties (profit and loss) that a contractor earns on other than cost-plus-award-fee (CPAF) contracts are based on objective measurements in terms of cost, performance, and schedule. The introduction of a subjective or even objective measure for reward or penalty, based upon security, would probably not provide a meaningful incentive to a contractor unless a preponderance of fee or profit was associated with it. This then could become counterproductive to the incentive placed on operational and funding aspects of the contract. Such an incentive would also be difficult, if not impossible, to administer and measure.

5. Attached hereto is a proposed contract article entitled, "Special Security Provisions" which highlights the importance we place on security in performance of the contract and sets forth the penalty a contractor is subject to in the event he fails to comply therewith. It should be noted that this article makes more specific certain rights which are inherent in the "default" and "termination" provisions of Government contracts. However, the article does include some language which may go too far in attributing the action of a contractor's employee

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to the contractor. Because we are, in effect, creating new contract provisions and inserting language which is not a part of existing procurement regulations, we have asked General Counsel to provide his comments on the enforceability and effectiveness of these provisions for your consideration, prior to implementation. Additionally, we should give consideration to soliciting industry comments in order to test acceptance of our contractors, which could possibly result in some beneficial suggestions.

/s/ John F. Blake

John F. Blake

Att

Distribution:

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Originating Office:

[Redacted Signature Box]

//James H. McDonald
Director of Logistics

15 JUN 1978

Date

TAB

SPECIAL SECURITY PROVISIONS

(a) The contractor shall maintain and administer, in accordance with industrial security manuals and agreements incorporated with the schedule of this contract, a security program which meets the requirements of these documents.

(b) Reference is made to the article of the General Provisions entitled "Default" ("Termination"). It is agreed and understood that failure of the contractor to maintain and administer a security program, fully compliant with the security requirements of this contract, constitutes grounds for termination for default.

(c) Specifically, the contract is subject to immediate default, without the requirement of a 10-day cure notice, where it has been determined by the contracting officer that failure to fully comply with the security requirements of the contract results from willful misconduct or lack of good faith on the part of any one of the contractor's directors or officers, or on the part of any of his managers, superintendents, or other equivalent representatives who have supervision or direction of:

(1) All or substantially all of the contractor's business, or

(2) All or substantially all of the contractor's operations at any one plant or separate location in which this contract is being performed, or

(3) A separate and complete major industrial operation in connection with the performance of this contract.

Reference is made to Article 24 of Section A of the General Provisions entitled "Non-Publicity." Violation of the terms and conditions of this clause by any employee of the contractor constitutes a major breach of contract, and the contract may be terminated immediately for default without the requirement of a 10-day cure notice.

(d) Where deficiencies in the contractor's security program are noted, the contractor shall be provided a written notice of these deficiencies and given a period of 10 days to take corrective action. If the contractor fails to take the necessary corrective action, the Government may terminate the whole or any part of this contract for default.

(e) The basis for the procedure (whether a 10-day notice is required or not) to be followed for termination of this contract under the provisions of this clause is a unilateral decision of the contracting officer and is not subject to the disputes clause of the contract. The factual basis upon which the default notice was issued is subject to the disputes clause of the contract.

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